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National City Monthly Letter on Business and Economic Conditions

New York, May, 1954

General Business Conditions

THE month of April has strengthened the impressions gained in March that the decline in business is flattening out. Latest available figures on industrial production and employment reveal little if any further slippage in overall totals, with a number of lines showing improvement. Department store sales throughout the country picked up sharply with the approach of Easter, and for the Easter season as a whole approximated the record volume of last year. These signs that the national economy is again finding a firm base after the downtrend since last summer, coupled with continued high building activity, strength in the commodity and security markets, and favorable earnings reports for the initial quarter by leading corporations, have had a cheering effect throughout the business community.

Industrial production, as measured by the Federal Reserve index (seasonally adjusted) decreased less than 1 per cent from February to March — about the same slight rate of decline as in the preceding two months. The first quarter decline was concentrated in the durable goods sector, reflecting some cutting back on defense goods production as well as a drop in steel and other metal fabricating industries.

Employment has shown similar trends, with a leveling off following the decline and with numerous plants recalling workers previously furloughed. Unemployment increased only slightly in March, according to the Bureau of the Census, while figures on unemployment insurance benefit claims extending through the first half of April have held practically unchanged since the early part of February.

Steel Operations Holding Steady

Further evidence of a tapering off in the industrial decline has been the maintenance of steel mill operations at around 68 per cent of capacity for the past two months, while steel scrap prices have firmed. New orders booked are reported currently as showing some slight improvement, and opinion in the industry seems to be that operations will hold around current levels or better. Weekly automobile production climbed to the highest rate since last August as producers competed for the crucial spring market. While retail car sales have been running less than 10 per cent behind a year ago, stocks of new cars in dealers' hands have continued heavy in anticipation of the usual seasonal increase in buying by the public. Agricultural implements, one of the first of the industries to feel the pinch in demand last year, have turned for the better, with employment in some plants back to the highest level in months. Production of synthetic texiles, on the other hand, was cut sharply last month because of unprofitable prices.

Aggregate sales and orders of manufacturers reporting to the Department of Commerce in-

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creased in March, and inventories continued to decline, all after seasonal adjustment. According to the National Association of Purchasing Agents, these same trends apparently continued in April. Forty-three per cent of the Association's member firms noted an increase in new orders, while only 17 per cent reported a decrease. One-third of the members increased production in April, while half held steady at the March level.

All this appears still very much in line with the "rolling adjustment" pattern which has characterized business at times since the war, and which so far has enabled it to experience periods of boom yet avoid the much-predicted major collapse.

Consumption Exceeding Production

While department store sales during the Easter season approximated those of a year ago, the same cannot be said of all retail sales, due especially to the lag in automobiles and other hard goods.

Aggregate consumption expenditures, including services as well as goods, for the first quarter of the year were at an annual rate of $230 billion against $228 billion in the first quarter of last year. The increase, however, went wholly for services. Expenditures on durable goods decreased 7 per cent, while those on nondurable goods were practically unchanged. Nevertheless, it would appear that, in general, consumer purchases of goods (as distinguished from services) have been running ahead of factory output, indicating that the corrective process of adjusting supplies to consumption is going forward.

The lag in buying of durable goods is not explained by lack of public spending power. Total personal income so far this year has been about the same as a year ago, with "disposable" income several billion dollars higher as a result of the reduction in personal income taxes on January 1. The answer is that people are saving their money and paying their debts, as shown by the rise in savings deposits, holdings of U.S. Savings bonds, etc., and the decline in consumer debt outstanding. Manifestly, it is up to business to coax the public to loosen up on its purse strings by producing the kind of goods that will appeal, by hard selling, and by attractive pricing.

New Records in Construction

The brightest spot in the business picture continues to be building construction. Month after month this goes on forging ahead to new high records. Contract awards for new construction of all kinds in March and during the first quarter were 13 per cent above a year ago, and preliminary data for April look good.

In plant and equipment expenditures, a new survey among the larger companies by the McGraw-Hill Publishing Company indicates business intentions to spend as much if not more money this year than they spent for these purposes during the previous banner year 1953. This is even more favorable than the results of a similar survey published a month earlier by the Department of Commerce and the Securities & Exchange Commission covering a larger sampling of business concerns.

Such findings are the most impressive evidence that could be had of continuing business confidence in the long-range outlook; and the plans, if carried out as scheduled, will have a powerful sustaining influence on the business situation generally. It is hard to envision any serious letdown in the face of so high a level of capital investment.

The Farm Outlook

Another large crop harvest is in prospect this year given favorable weather, despite curbs on acreage of several major crops. Plantings of 59 principal crops are estimated by the Department of Agriculture at 356.5 million acres, only 2.7 million under 1953. With no restrictions on their use, some 20 million acres diverted from cotton, wheat, and corn are being planted to other crops, mainly soybeans, flaxseed, oats, barley, grain sorghums, and rice. Also tending to keep plantings high is the fact that producers may under the government program secure price support on a specified crop, even though they do not comply with restrictions for other controlled crops grown on the same farm.

Many farmers who feed most of their corn production have little interest in price support on that crop and are expected to plant about as much as last year. In addition, continued price support at 90 per cent of parity on the basic crops will encourage farmers to use more fertilizer and other intensive crop practices.

Despite the generally favorable crop outlook, drought and dust storms have hurt prospects in some areas. Conditions are particularly serious in the Southwest and Central Great Plains, and were mainly responsible for the Department of Agriculture reducing its estimate of the winter wheat crop, as of April 1, about 10 per cent below last December's forecast. Since then rains have provided some relief.

According to the Soil Conservation Service, most of the 3.5 million acres put under the plow since 1942 in five southwestern states, where the drought is most acute, should never have been put in crops anyway. This uneconomic cultivation is another one of the bad results of high price support policies and other farm subsidies. Not only did this extra crop production aggravate present surpluses, but plowing of the land made it vulnerable to dust storms and loss of valuable topsoil.

The Crop Storage Problem

Due to large carryovers of old crops, particularly corn, wheat, and cotton, coupled with prospective heavy production this year, agriculture may be faced with its most serious storage problem in history. Even last year storage facilities were stretched to the limit, and in some areas price support temporarily was permitted on grain piled on the ground or in structures normally considered unfit for storage. Another emergency measure was the use of 125 merchant ships of the reserve fleet to store wheat.

In order to encourage the construction of new and the expansion of existing storage facilities, the Congress last year authorized accelerated amortization of the cost of new warehouses built by cooperatives and commercial warehousemen. In addition, the Department of Agriculture has extended through June 30, 1955 its program of lending the money to build more on-farm storage facilities. Much of this additional capacity, however, is not expected to be available in time to be used this year. As a result, the Department of Agriculture has purchased additional storage capacity and has arranged for the use of more ships. In an effort to ease the squeeze of CCC and commercial storage, the Government announced that farmers holding certain 1952 and 1953 crops under loans and purchase agreements will be permitted to reseal these commodities and earn a storage payment equivalent to commercial warehouse charges for so doing.

Farm Price Decline Levels Off

Average prices received by farmers in mid-April, as computed by the Department of Agriculture, were only slightly below a year previous and some 3 per cent above mid-June 1950, just before Korea. Farm costs, however, were slightly above a year earlier, thereby reducing the overall "parity" ratio of prices received by farmers to prices paid from 92 to 91 per cent.

While corn and wheat generally have been selling well below support levels, non-supported hogs, which two years ago were selling around 76 per cent of parity, sold in mid-April at 128 per cent. The high price reflects the cut in hog numbers resulting from low prices in 1952, demonstrating that the law of supply and demand is still effective when permitted to operate. Had a hog price support program been instituted, the CCC today might be loaded with surplus pork and lard among its other inventories. In all likelihood, hog producers today would be receiving sharply lower prices.

Cattle prices, despite a further upturn in numbers to a new high, have shown encouraging strength. Reflecting reasonable retail prices, consumer demand for beef has continued strong and kept stocks low. While the Government last fall and winter purchased 865,000 head of cattle to lessen the strain on markets, it now appears that the cattle industry, barring a severe drought, is on its way to solving its problem without reliance upon direct supports on live cattle.

Overall cash receipts from farm marketings, totaling about $6.6 billion during the first quarter of 1954, were 3 per cent below last year. With farm costs likely to stay high, farmers' net income this year is expected to run about 5 per cent under the 1953 figure of $12.8 billion. Although marketings may approach last year's level, average prices received by farmers may be lower because of depressing surpluses. Lower supports for some items, particularly dairy products, also may cut net income. The most important factor bearing on farm income will, of course, be the trend of general business during the year.

First Quarter Corporate Earnings

Reports of manufacturing corporations for the first quarter issued to date show that, despite generally lower production and shipments, combined net income declined only moderately from the preceding quarter and increased slightly as compared with the first quarter a year ago. The showing, however, is extremely mixed, with the number of companies having increases in net income after taxes about equalling the number with decreases. Sharply lower federal tax reserves this year, resulting in part from expiration of the excess profits tax at the end of '53, had a widespread effect of cushioning or more than offsetting the declines in operating income.

Railroads and airlines experienced some decline in traffic and earnings as compared with the first quarter a year ago, but most of the electric, gas, and telephone utilities continued their long-term upward trends of both gross revenues and net income.

NET INCOME OF LEADING CORPORATIONS FOR THE FIRST QUARTER

(In Thousands of Dollars)

No. of Cos.	Industry Groups	Reported Net Income After Taxes First Qr. 1953	Fourth Qr. 1953	First Qr. 1954	Per Cent Change From First Qr. 1953	Fourth Qr. 1953
25	Food products	$ 26,720	$ 31,484	$ 29,330	+10	— 7
14	Beverages	10,561	16,306	8,465	—20	—48
10	Tobacco products	15,523	17,477	17,122	+10	— 2
28	Textiles and apparel	22,269	14,385	14,586	—35	+ 1
23	Paper and allied products	22,573	26,018	27,172	+20	+ 4
36	Chemical products	147,622	144,431	158,051	+ 7	+ 9
17	Drugs, soap, cosmetics	28,679	28,484	32,250	+12	+13
28	Petroleum producing and refining	396,666	488,453	451,252	+14	— 8
32	Cement, glass, and stone	38,762	42,103	35,740	— 8	—15
34	Iron and steel	149.788	162,374	123,315	—18	—24
16	Building, heating, plumbing equipment	14,708	24,939	15,509	+ 5	—38
20	Electrical equipment, radio and television	62,215	80,878	83,829	+35	+ 4
44	Machinery	30,613	31,188	33,917	+11	+ 9
9	Office equipment	14,554	18,398	18.051	+24	— 2
9	Automobiles and trucks	159,285	148,036	184,463	+16	+25
29	Automobile parts	30,866	27,070	26,382	—15	— 8
18	Railway equipment	13,684	15,319	15,516	+13	+ 1
79	Miscellaneous metal products	96.490	95,996	102,804	+ 7	+ 7
39	Miscellaneous manufacturing	57,675	68,698	60,521	+ 5	—12
505	Total manufacturing	1,339,253	1,482,037	1,438,275	+ 7	— 3
25	Mining and quarrying	19,726	24,421	20,072	+ 2	—18
24	Trade (retail and wholesale)	14,472	31,116	12,703	—12	—59
16	Service and amusement industries	16,536	12,513	10,958	—34	—12
570	Total	$1,389,987	$1,550,087	$1,482,008	+ 7	— 4

Our tabulation of 570 reports, comprised principally of the larger manufacturing organizations but including also a limited number of companies in the mining, trade, amusement, and service industries, shows for the first quarter a combined net income of approximately $1,482 million after taxes. This is 4 per cent under the preceding quarter, but 7 per cent above the first quarter of last year. The trend of the quarterly totals during the past two years has been as follows:

Net Income After Taxes of 570 Leading Corporations

(In Millions of Dollars)

	1952	1953	1954
First quarter	$1,281	$1,390	$1,482
Second quarter	1,200	1,491	
Third quarter	1,229	1,484	
Fourth quarter	1,614	1,550	

Contrasting with the relative stability in the combined totals of net income, the figures covering major industries as given in the summary above show considerable fluctuation.

The fluctuations shown in net income this year reflect new variations in the impact of numerous different factors, favorable and otherwise. There was a decline in the dollar sales billed in the first quarter as compared with a year ago for slightly over half of the reporting companies. In some cases this decline indicated a let-down in consumer demand for products following the Korean war boom; in some, curtailed buying by retail and wholesale distributors desiring to work down their inventories; in others, cut-backs or termination of shipments under government defense contracts. With shortages and sellers' markets virtually ended, competition has become more intensified all along the line.

At the same time, business continues to operate in the face of a persistent tendency for costs to advance. While such costs could be absorbed when sales were pushing ahead to set new high records year after year, they become more serious when sales turn downward and costs cannot be cut correspondingly. This has been reflected in a sharp decline in operating earnings, before income taxes, of the companies that have published statements.

An offsetting factor has been the lowering in the federal tax load in the expiration of the excess profits tax at the end of 1953. That wartime revenue measure imposed taxes at the rate of 82 per cent on the portion of corporate income defined as "excess" over a specified base of earnings or a return upon invested capital. Effective January 1, 1954, corporate income became subject only to the combined normal tax and surtax rate amounting to 52 per cent (with lower rates on the first $25,000 of taxable income and where there are capital gains and depletion allowances). Although federal tax rates are below their recent peaks, they still take half of most companies' earnings. By comparison, the corporate rate in 1939 was 18 per cent, in 1929 11 per cent, and in 1913 when the federal income tax first went into effect only 1 per cent.

Technically, the federal tax rate this year under existing law was 52 per cent for the first quarter only and declined on April 1, 1954 to 47

per cent, which rate is to apply to the remaining three quarters and would mean in practical application an average rate of 48¼ per cent for the full year. Congress has virtually agreed, however, to extend the 52 per cent rate for one more year and has written a provision to that effect into the Internal Revenue Code revision bill already passed by the House. On the assumption that this extension will be enacted into law in due course, it is understood that accountants generally are continuing this year to use the 52 per cent rate as the more realistic.

Following is a condensed summary, partly estimated, of the sales, income taxes, and net income reported by the 505 manufacturing companies in our tabulation:

Sales and Net Income of 505 Manufacturing Corporations in the First Quarter

(In Millions of Dollars)

	1953	1954	Change Amount	Change %
Receipts from sales, etc.	$24,550	$23,209	—1,341	— 5
Total costs, except taxes	21,075	20,332	— 743	— 4
Balance before taxes	3,475	2,877	— 598	—17
Federal income & e. p. taxes	2,136	1,439	— 697	—33
Net income after taxes	1,339	1,438	+ 99	+ 7
Taxes to balance before taxes	61%	50%		
Net income per sales dollar	5.5c	6.2c		

It will be noted that, on a decrease in dollar sales billed of 5 per cent, the income balance after all costs except taxes was cut 17 per cent. Of this balance, federal income taxes absorbed an average of 50 per cent this year, against 61 per cent in the first quarter of '53. The decline in tax liability, amounting to 33 per cent, more than offset the decline in operating earnings and brought about an increase of 7 per cent in the net income after taxes.

In general, the greatest tax relief was received by companies having the most vigorous record of growth, which in the past had been paying the heaviest excess profits taxes. At the other extreme are large numbers of companies which had not been very profitable, experienced a decline in operating earnings this year, and were unable to share in much relief from the expiration of a tax to which little if any of their income had been subject.

Discount Rate Cut Again

The Federal Reserve Bank of Chicago reduced its discount rate from 1¾ to 1½ per cent effective April 14. The New York and San Francisco Banks followed suit effective April 16 and by April 29 a 1½ per cent rate had been established for nine of the twelve Reserve Banks. A Federal Reserve spokesman characterized the reduction as a reaffirmation of the established policy of "active ease" in the money market and another step toward narrowing the spread between discount rate and short-term money rates. The further discount rate reduction came only two and a half months after the cut from 2 to 1¾ per cent discussed in the March issue of this Letter.

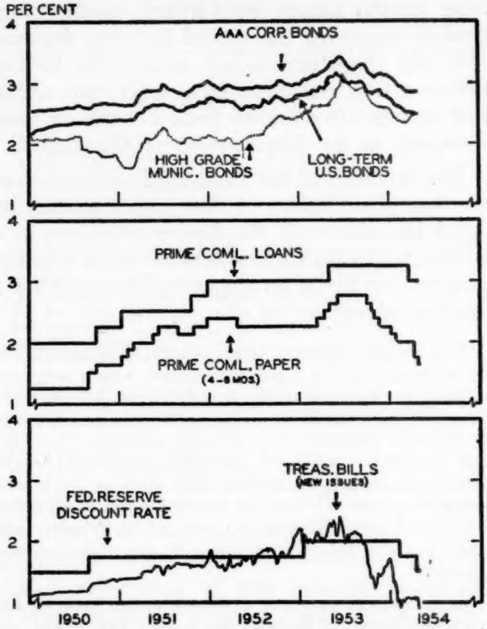
The Secretary of the Treasury, speaking before the American Society of Newspaper Editors on April 15, mentioned the discount rate cut as a further action the Government has taken over the past year to insure an ample credit supply for a growing economy:

> The Federal Reserve Board — with its responsibility for monetary policy — reduced reserve requirements of member banks substantially as early as last June to make sure that there would be no bar to the proper volume of bank credit necessary to a growing economy. The Federal Reserve has purchased short-term government securities in the market, to increase bank reserves, for a considerable period. The rate at which bankers can borrow from the Federal Reserve was reduced in February and again just day before yesterday a further reduction was approved. . . .
>
> In the current economic environment the Treasury has purposely done its financing in a way that would not interfere with the availability of long-term investment funds to corporations, state and local governments, and for mortgages to home owners. We want to be sure that plant and equipment, home building, and other construction all have ample available funds. The fact that construction thus far this year is running so high demonstrates how effective these policies are.

The Secretary at the same time decried "the prophets of gloom" who are looking for a major depression, cited the near-record levels of personal income and employment during the first quarter of the year, and expressed his confidence in the future.

Narrowing the Spread

The stabilizing trends in the business situation, and the active absorption of credit in construction, led some observers to question the wisdom of another shot of easy money at this time. The best case for the further discount rate cut was not based on clear symptoms of further weakening in business but rather on the technical ground that the spread between discount rates and short-term money rates should be narrowed. The discount windows at the Federal Reserve Banks have been comparatively neglected by the banks in recent months since, as the chart indicates, it has been possible for banks holding Treasury bills to sell them with a loss of income of around 1 per cent or ¾ per cent less than they had to pay on borrowing from a Federal Reserve Bank. As a general rule Treasury bill yields hold within ½ per cent of the discount rate.



Bond Yields and Money Rates, Weekly Through April

As the discount rate cuts were being posted the Treasury disclosed plans for $3 billion financing to cover cash requirements up to the June 15 tax period. One billion was borrowed April 27 by the sale of 52-day Tax Anticipation Series Treasury bills, due June 18, at a cost of 0.73 per cent, a record low new-money borrowing cost for the postwar period. Two billion is being sought on 4¾ year 1⅞ per cent notes to be sold May 4 for payment May 17. Holders of the $4.9 billion 2⅝ per cent certificates due June 1 will be invited to take in exchange similar notes or 1⅛ per cent certificates due May 17, 1955. Holders of the remnants of three bond issues due June 15, totaling $2.4 billion, will be offered 1⅛ per cent certificates in exchange. Most holders of these bonds took the opportunity back in February to make an exchange for 2½ per cent bonds of 1961.

The regular weekly 91-day Treasury bill issues were placed during April at rates between 1.07 and 0.89 per cent, the same range that had prevailed during February and March.

A Puzzling Question

Why Treasury bill yields have fallen so far is a question that has puzzled many people. The Federal Reserve, through open market operations, has been maintaining $400 to $500 million of free excess reserves among the banks, a situation that tends to keep bill yields below the discount rate. But this is not a complete explanation. Two years ago when free excess reserves were running near a half billion level Treasury bill yields were averaging only ⅛ per cent below the discount rate, then 1¾ per cent.

One influence toward low bill yields has been a tendency of the market to anticipate further actions to ease credit. Since January the market has been living in momentary expectation of early action to reduce cash reserve requirements of the banks. Unlike the discount rate, the banks' cash reserve requirements, while eased last June, remain at a comparatively high level. It has seemed reasonable to expect some relief on this score, freeing additional funds for lending or investing.

Among other factors which may explain the depressed level of bill yields are the fixed habit of many banks and corporations to keep excess funds invested almost regardless of rate, the unavailability since October of the Treasury Savings notes formerly on sale, the strengthening of business cash positions by inventory reduction, and, last but not least, the February 15 Treasury refunding which reduced the outstanding supply of short-term Treasury obligations.

Effects of Bill Yield Level

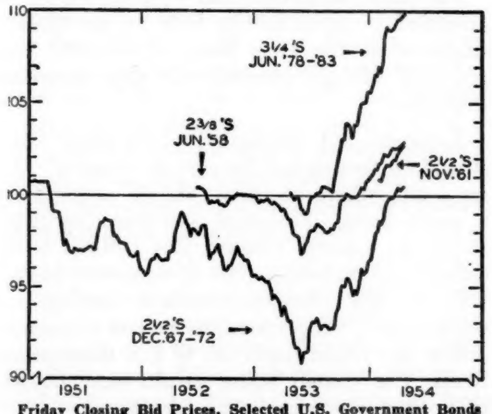
The depressed level of Treasury bill yields has been a prime mover in the great bull market for bonds since it has put banks under a practical compulsion to buy intermediate and longer-term obligations to realize an adequate return. It also has had diverse other effects. Large corporations, dissatisfied with the return they get investing surplus funds in bills, have placed time deposits with banks, enlarging the investment problem of the banks; they have bought commercial paper (negotiable short-term notes of sales finance companies, merchants, food processors, etc.); and they have offered loans to government security dealers in competition with the banks. As the chart shows, funds seeking commercial paper investments have pulled the rate down to 1⅝ per cent, increasing the temptation of borrowers to supply their needs through this channel rather than through bank loans. The amount of commercial paper outstanding at the present time is estimated at $2 billion of which three-quarters is represented by sales finance company borrowings.

To improve their outlets for temporary surpluses of funds, the New York banks in April inaugurated a new call loan rate, fluctuating generally between 1 and 1½ per cent, depending on the reserve position of the banks. The rate is applicable to overnight loans to government security dealers collateralled by Treasury bills or other U.S. obligations of short term.

The depression in these short-term open market money rates, along with deposit growth, have created an intense pressure on banks to seek loans paying more adequate rates as well as to acquire intermediate and longer-term bonds. Considering the inventory reductions that have been in progress, and the slack demands that normally follow the March 15 tax date, bank loans to business have been well sustained. Fluctuations since January have more or less followed the expected seasonal pattern. Consumer instalment credit declined in January and February, in response to seasonal influences and a slower rate of buying of cars and appliances.

Bond Market

The bond market showed signs of fatigue in April after its violent bull movement. The long-term Treasury market, which has not been called upon to absorb any new offerings, has continued on a rising price trend although the advance has been slowed by a combination of profit-taking and switching of investor preference to mortgages, State and municipal obligations, and stocks. As one byproduct of the drop in yields on marketable bonds, sales of U.S. Savings bonds have improved to the best levels since 1950.



Friday Closing Bid Prices, Selected U.S. Government Bonds Last Plotting for Thursday, April 29

As the chart shows, the Treasury 3¼s of 1978-83, which reached 109 the first of March, touched 110 at the close of April. The War Loan 2½s of 1967-72 held around 100½. The new 2½s due November, 1961, issued February 15 and a favored bank investment, rose 1⅛ points, reaching 103.

The superior strength of bonds within ten years to maturity reveals the importance to the U.S. bond market of the pressure built up on the banks to reach out. The natural sources of strength, in the shape of yields attractive to pension funds and savings institutions, have faded. Insurance companies, savings and loan associations and mutual savings banks have found employment for substantial funds in mortgages and in turnpike and other State and local government bonds — in other words financing the construction boom.

Offerings of State and local government bonds came along so fast in February and March that dealer inventories were built up to levels requiring general price markdowns in early April. After an improvement in yield to the investor of ⅛ to ¼ per cent, the absorptive capacity of the market improved. Evidently because of the competition offered by the mortgage and tax-exempt markets, corporate bond flotations, although scheduled at a lower volume than last year, have encountered stiff sales resistance when underwriters have attempted to place bonds at yields below 3 per cent.

An Historic Swing

The drop in yields on top-grade bonds since last spring now runs close to ¾ per cent. Declines in bond yields of this magnitude over a single year's span have been rare in history and have generally been associated with an emergence from serious panic or crisis, as in 1921-22 and 1933-34. The swing reflects not only the strain under which the market was laboring a year ago but the power the Federal Reserve has thrown into its effort to speed credit expansion and turn the recession.

It is a question whether, in trying to make credit still easier, long-run dangers do not counterbalance short-term benefits. The law of diminishing returns applies to repeated dosages of easy money. And surplus funds are easier to put in than to take out, as the experiences of 1927-29, 1933-37, and 1942-53, so well demonstrate. Neither the Federal Reserve, the banks, nor the public should relish the memory of these experiments.

U.S. Foreign Economic Policy

On March 30 President Eisenhower submitted to the Congress his long-awaited message outlining specific proposals for an overall U.S. foreign economic program, including trade and investment policy. These proposals, implementing the Randall report issued in January, the Administration believes to be best calculated to promote the welfare and strength of this country and of the free world. This message is historic as marking the first time the Congress has been asked to take definite legislative action upon a program covering, and seeking to coordinate, all phases of our foreign economic policy.

What has brought the whole question of our foreign economic policy to a head was the scheduled expiration of the Reciprocal Trade Agreements Act last June. Faced with this major policy problem within six months after taking office, the new Administration recommended, and the Congress approved, legislation extending the Trade Agreements Act for another year. The legislation also established a Commission on Foreign Economic Policy, generally known as the Randall Commission after its chairman, Clarence B. Randall, chairman of the board of the Inland Steel Company, "to examine, study and report on the subjects of international trade and its enlargement consistent with a sound domestic economy, our foreign economic policy, and the trade aspects of our national security and total foreign economic policy." Its report was received with intense interest, both in this country and abroad, as offering a preview of the course that Administration policy might take.

The President's Recommendations

The President's recommendations to the Congress are, as was generally expected, closely in line with those of the Randall Commission. Characterizing his proposals as a "minimum program" of interrelated parts, each requiring the other, the President stated:

> Conceived as a whole, this program consists of four major parts: aid — which we wish to curtail; investment — which we wish to encourage; convertibility — which we wish to facilitate; and trade — which we wish to expand.
>
> . . . we and other free nations are still severely limited by the persistence of uneconomic, man-made barriers to mutual trade and the flow of funds among us . . . The solution is a higher level of two-way trade. Thus we can sell and receive payments for our exports and have an increasing volume of investment abroad to assist economic development overseas and yield returns to us.
>
> . . . Failure so to move will directly threaten our domestic economy. For it will doom our efforts to find ways by which others, through their own efforts, can buy our goods. The only practicable alternative is to reduce exports . . . Our domestic employment, our standard of living, our security, and the solidarity of the free world — all are involved.

"More Trade, Less Aid"

Following is a summary of the major recommendations dealing with "more trade, less aid":

The Trade Agreements Act, now due to expire June 12, 1954, should be extended three years, with authority for the President to (a) reduce tariffs by 5 per cent of present rates in each year: (b) to reduce to 50 per cent ad valorem over a three-year period any rates in excess of that ceiling; and (c) on products imported in negligible amounts or not all, to reduce tariffs by one-half the rates in effect January 1, 1945, such reductions to be spread over three years.

The present "peril point" and "escape clause" procedures, whereby minimum or increased tariff rates may be prescribed when domestic industries are injured by foreign competition, should be retained, though with the authority of the President expressly reaffirmed to set aside findings under these provisons when he considers such action to be in the "national interest".

In defining "unfair competition", mere differences in wage levels should not necessarily govern, but tariff reduction should be withheld on products made by workers receiving wages which are substandard in the exporting country.

In the case of raw materials, tariff policy should afford "reasonably easy" access to the U.S. market. Domestic sources of supply for materials required for military purposes should be assured by "direct" means (subsidies) rather than by tariffs or quotas.

Commodity definitions and tariff rates should be simplified to reduce difficulties and delays involved in the determination of tariffs.

The "Buy American" Act of 1933 should be amended to treat foreign bids on government contracts on the same basis as domestic bids, provided foreign governments give reciprocal treatment.

Economic aid, particularly on a grant basis, should be terminated "as soon as possible". Military aid, where required, should continue on a grant basis. Technical assistance programs should be carried forward, but without heavy outlays and without capital investments. In general, foreign countries desiring development capital must look primarily to private investment and to the World Bank, not to U.S. Government funds. The United States should ease duplication of taxes on income earned abroad.

The President and the Randall report both pointed out that American farm policy should harmonize with foreign trade policy, and that inflexible price supports should be abandoned.

International price stability should be encouraged, not by commodity agreements, but by liberalizing trade, by encouraging diversification in foreign economies, by avoiding disruptive action in our commodity and stockpiling programs, and by policies which temper fluctuations in the domestic economy.

To facilitate international currency convertibility, the United States, the President stated,

favors more active use of the International Monetary Fund and possibly stand-by credits by the Federal Reserve Banks. Proposals, mainly advanced abroad, for setting up a huge government exchange stabilization fund (requiring additional budgetary appropriations) were rejected.

Opposing Viewpoints

The foregoing highly condensed summary will give some idea of the scope and complexity of the task to which the Administration has addressed itself. The trouble is that, while all can agree as to general objectives, there are widespread and deep-seated differences of opinion on how to reach them. Most of the specific proposals involve, as the reader will readily perceive, a veritable bramble patch of controversy.

This is particularly true of the recommendations for reducing trade barriers. On one side are large and important business groups who regard tariff protection as vitally essential to equalize differences in wage costs here and abroad. They bitterly oppose any lowering of tariffs as posing a grave threat to the domestic economy. Without adequate tariff protection, many industries, they warn, would be unable to compete with foreign goods produced at lower cost, thus throwing American workers out of jobs, curtailing purchasing power, and spreading depression. The supply of many items essential to our national defense would be imperiled if we should become too dependent upon foreign sources. With competition everywhere increasing as the period of postwar shortages passes, these fears have become intensified.

On the other side are equally large and important business groups, including importers and many of our mass production industries doing business all over the world, who take the opposite view. Apart from such special interest as individual concerns may have in securing freer access to foreign sources of supply, these groups base their case primarily upon the broad principle of encouraging the growth of multilateral trade in which all can participate. They point out that unless we are willing to adopt more liberal trade policies, other countries will be unable to pay for the goods they need from us for their progress and development, and which we need to sell to them if we are to find a full market for the increasing output of our farms and factories. This need for making dollars more readily available through a freer flow of trade is, they urge, all the more important now that we are cutting down foreign aid and give-away programs and thus relieving the heavy burdens on the American taxpayer.

Even in the same industry some companies will be on one side of the fence and some on the other, depending on whether their source of supply is mainly domestic or foreign. Different departments within a single company may have diametrically opposed views.

This dependence upon sales abroad is found in some of our most protectionist-minded industries. Thus, while cotton manufacturers have gone on record against any reduction in existing tariffs, it has been made clear that they too have a stake in maintenance of foreign outlets. Matthew J. Cuffe, president of the Textile Export Association of the U.S., speaking at a meeting of the American Cotton Manufacturers Institute last month, pointed out that since 1947 more than 6,000,000,000 yards of American cotton textiles have been shipped abroad. This volume, he said, has been one of the factors which have made it possible for the American industry to operate its equipment at a rate far in excess of the prewar average and to pay the highest textile wages in the world.

Criticisms of the Program

Obviously the Randall Commission faced a tough assignment. Not only was opinion at large and in the Congress sharply divided, but also in the Commission itself.

The result has been a program of compromises which has encountered criticism from advocates of freer trade and protectionists alike. On the protectionist side, it has raised a storm of protest as going too far and opening the gates to a flood of cheaply-produced foreign merchandise that would be disastrous to domestic producers. On the trade liberalist side, and in many quarters abroad, it has been criticized as not going far enough, with each concession so hedged about with safeguards and restrictions as to fall far short of what is really called for.

An example of the latter reaction was the critique of the Randall report by seventeen economists attending a conference at Princeton University last February. While agreeing with the report in numerous particulars, the economists nevertheless criticized the recommendations on commercial policy as inadequate on various counts, including especially the retention of such loopholes as the "peril point" and "escape" clauses. They deplored the report for want of basic philosophy and for failure to develop a long-term policy for assisting underdeveloped areas.

With due respect for the viewpoint represented in the Princeton critique, and for that of our foreign friends, which would have this country move faster in the adoption of liberal commercial policies, there is no use shooting for the moon. Even the Princeton group agreed that "if all the recommendations on trade policy made by the Randall Commission were enacted by the Congress in the next one or two years, the result would constitute the biggest single step towards a more liberal commercial policy since the Reciprocal Trade Agreements Act was passed in 1934."

To serve a practical purpose the Randall Commission had to work out a program upon which a majority of its members could agree and upon which the Congress and the country could go along. Such a program, considering the conflicting views, could not be other than a compromise. Two members of the Commission — Representative Reed, chairman of the House Ways and Means Committee, and Representative Simpson — submitted a sharply dissenting minority report and Senator Millikin, chairman of the Senate Finance Committee, filed a long statement expressing reservations or clear dissent on a number of recommendations.

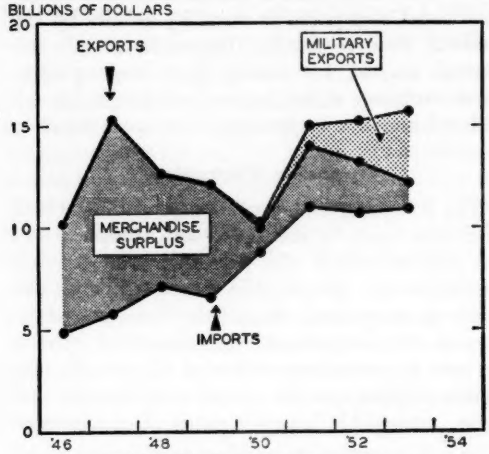
Thus the real test of the Randall report, and of the President's proposals based upon it, is not whether the program is ideal, but whether it offers a middle ground upon which a majority of fair-minded people can stand. That of course remains to be seen.

Progress Towards Balanced Trade

Pertinent to this question of "more trade, less aid" is a review of what has actually been occurring in our balance of payments with the world at large.

It may come as a surprise to many to learn that, at least for the time being, the period of huge export balances which characterized U.S. foreign trade in the first years after the war has come to a close. As shown by the accompanying chart, this was brought about mainly by increased imports. In 1953 imports totalling almost $11 billion were only $1.3 billion short of exports (exclusive of military aid) for the same period.

That is for merchandise trade alone. Counting the usual "invisible" items in the balance of payments (tourist expenditures, shipping, insurance, dividends and interest, etc.), plus the huge sums spent by our military forces abroad — altogether netting foreign countries over $1 billion on balance — it appears that in 1953 our overall trade and service accounts with the rest of the world were about in equilibrium. If anything there was a small deficit for the United States. Temporarily at least the much talked of "dollar gap" has been closed.



United States Foreign Trade by Years

With the additional dollars flowing abroad in the form of government economic aid and private capital transactions, the so-called dollar shortage has given way to a substantial dollar surplus. Foreign countries have been enabled to build up their gold and dollar reserves at a rate currently running in excess of $2 billion a year.

A Precarious Balance

The Randall Commission agrees that this is an "impressive record", but warns against concluding prematurely that the "dollar problem" has been solved. Among other things, it calls attention to the present limitations abroad on dollar imports and argues that, in a free market and with convertible currencies, the potential demand for dollar goods and services might substantially exceed the present restricted demand. It points, particularly, to the fact that the building up of foreign gold and dollar reserves has been made possible in large measure by U.S. Government economic aid and extraordinary military expenditures abroad at the rate of some $5 billion a year. A decline in these expenditures might, it is implied, again bring back the old problem of the "dollar gap".

Nor does the Commission entertain much hope that expansion of private investment can fill this gap, since "many of the deterrents can be overcome only gradually".

A Heavy Responsibility

Thus we come back to the main premise of the Randall report and of the President's proposals: that preservation of equilibrium in the balance of payments and maintenance of U.S. export sales at a high level will require a further growth of U.S. imports.

This places a heavy responsibility upon the policy-makers in the Congress and the Administration. Maintenance of exports is, as we have pointed out earlier, important to agriculture and to many branches of industry. The aggravation of our present farm surplus problem, brought about by the slump of about one-third in agricultural exports in the past two years, is a forceful reminder of this fact. Because of the need of foreign countries to conserve dollars, our total commercial exports dropped from $14.0 billion in 1951 to $12.2 billion in 1953, reducing the market for American goods and pointing up the need to achieve international balance by an expansion rather than a restriction of trade.

On the other hand, any substantial lowering of tariffs to encourage imports would have adverse effects upon industries dependent upon tariff protection.

The United States has already gone a considerable way in reducing tariffs since the Reciprocal Trade Agreements Program was inaugurated in 1934. At that time our tariffs amounted to 50 per cent of dutiable imports; today they average about 12 per cent. About 55 per cent of imports now are duty-free. While these figures conceal some rates which are higher, and do not indicate the extent to which such rates excluded goods that might otherwise have come in, there appears ample justification for the statement in the Randall report that, "the United States is no longer among the higher tariff countries of the world."

But expansion of trade is dependent on more than one factor. The fact that rising imports have been possible in recent years under present tariff rates would seem to indicate that there has been some tendency in current thinking both here and abroad to exaggerate the weight of the American tariff upon trade. Clearly, prosperity in the United States market, together with recovery and higher production abroad, have been the predominant influences in increasing imports. This, of course, is no reason for assuming that the situation will take care of itself in ways that will be comfortable for everyone. In one way or another adjustments will have to be made, and it would be a good deal to expect that they can occur without somebody getting hurt in the process.

This being so, the key question is where the chief emphasis should be put in working out more liberal trade policies. It is important from the standpoint of our foreign friends to see a more stable and permanent pattern emerging. One factor which deters foreign business concerns from seeking to develop the American market is fear of new tariff and trade restrictions in the future. Foreign success in the American market, even on a fair competitive basis, has too often given rise to attempts to erect new trade barriers — at a loss not only to the foreign seller but also to the American consumer, who thereby fails to benefit from advancing efficiency and ingenuity abroad.

It is one thing suddenly and arbitrarily to cut the ground from under important industries whose development has been fostered by tariff protection, and another thing to undertake to protect such industries by further raising tariffs whenever foreign exporters, because of improved products, lower prices, or better salesmanship, are able to overcome the original tariff handicap. In the opinion of many trade experts, repeal of the "escape" procedure of the Reciprocal Trade Agreements Act, along with customs simplification and modification of the "Buy American" Act, are as important as lower tariffs in encouraging trade, and would be less disturbing in their effects.

But establishment of a dependable international balance is not something the United States can accomplish alone. The problem must, as the Randall report states, be attacked on many fronts, and too much dependence should not be placed on any one line of attack. "The final solution", the report declares, "will probably depend even more upon the efforts of other countries than upon our own. It will involve their continuing internal efforts to achieve sound and strong economies and their external efforts to correct their international imbalance." When all is said and done, the fact remains that the greatest contribution this country can make is the maintenance of a full measure of production and consumption at home.

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